A COMPARATIVE ANALYSIS OF CORPORATE GOVERNANCE CODES IN AUSTRALIA, CHINA AND INDONESIA

Dr Xinting Jia*
Centre for International Corporate Governance Research
Victoria University
Melbourne, Australia
Email: xinting.jia@vu.edu.au

Professor Anona Armstrong
Centre for International Corporate Governance Research
Victoria University
Melbourne, Australia
Email: anona.armstrong@vu.edu.au

Preferred stream: 15 Sustainability and Social Issues in Management:

Profile: Dr Xinting Jia is a Research Officer at the Centre for International Corporate Governance Research of Victoria University, Melbourne. Her research interest is on corporate governance in listed companies in the Asia-Pacific region. Xinting completed her PhD in corporate governance in 2006, and her thesis was focused on a comparative analysis of corporate governance practices in listed resources companies in China and Australia. The leading UK publisher, Routledge, has agreed to publish a book based on Xinting's PhD thesis.

Profile: Professor Armstrong is the Director of the Centre for International Corporate Governance Research at Victoria University, Melbourne. Her research and supervision interests are corporate governance, ethical climate and corporate social responsibility. Professor Armstrong is a Past President and Life Member of the Australasian Evaluation Society and was elected a Fellow of the Australian Psychological Society, is a Fellow of the Australian Institute of Company Directors, and is a Life Member of Clare Hall at Cambridge University.

A COMPARATIVE ANALYSIS OF CORPORATE GOVERNANCE CODES IN AUSTRALIA, CHINA AND INDONESIA

ABSTRACT

Corporate governance codes and standards proliferated around the world after collapses of major corporations in 2001. While most of the corporate governance codes are built upon the Organisation for Economic Co-operation and Development (OECD) Principles of Corporate Governance (issued first in 1999 and subsequently revised in 2004), there are some major differences among various standards to reflect each country's own unique circumstances. This paper is focused on a comparative analysis of corporate governance standards in Australia, China and Indonesia. It provides insights on similarities and differences in corporate governance codes in these three countries and illustrates how countries with different political, economic and social regimes have adopted the code to suit their own development stages. It also illustrates that while the regulators are not prescriptive about how the codes should be adopted, implementing the codes has encouraged good corporate governance behaviour among the countries analysed in this paper.

Keywords: corporate governance, corporate governance codes, corporate governance standards and corporate governance principles

INTRODUCTION

Corporate governance problems have existed ever since the formation of modern corporations (Rafferty, 1999), as suggested by the following statistics:

> By 1886, …, almost one in three public companies which had incorporated after the enactment of limited liability legislation in England in the 1850s had ended in insolvency, in many cases presumably related to corruptions of various kinds (Rafferty, 1999: 154).

Despite some of the problems, the phrase 'corporate governance' has been in circulation for only about twenty years (Zingales, 1998; Farrar, 2005: 3), and the recognition of problems emerging from the separation of ownership and control goes back to 1932 (Berle and Means, 1932).

According to the Organisation for Economic Co-operation Development (OECD) Principles of Corporate Governance (OECD, 2004: 11), corporate governance can be defined as a system that "involves a set of relationships between a company's management, its board, its shareholders and other stakeholders". In recent years, research on corporate governance has developed into a multidisciplinary area. At micro-level, it has focused on relationships between the shareholders, the board and the management; and at macro-level, it involves legal control (the so called 'black letter law'), Stock Exchange Listing Requirements, Statements of Accounting Practices, Code of Conduct, Corporate Governance Principles and Guidelines, Statements of Best Practices (these may be called ‘soft’ law) and Business Ethics (Farrar, 2005). This paper chose to focus on corporate governance standards.

In 2001, scandals in the US (Enron, Worldcom) have been a major concern of corporate governance around the world. At the same time, stock exchanges were also concerned about the aftermath of collapses of major corporations – the potential damage to shareholder confidence. Under this circumstance, various corporate governance codes and principles were introduced to provide guidance to company boards and their directors on good governance practices; many of those codes and principles have their origins in the Organisation for Economic Co-operation and Development (OECD) Principles of Corporate Governance, first introduced in 1999. This applies to the Corporate Governance Codes and Principles introduced in Australia, China and Indonesia.

The purpose of this paper is to compare corporate governance codes in the three countries, Australia, China and Indonesia. The Australian Stock Exchange (ASX) introduced the Australian Principles of Good Governance and Best Practices Recommendations in 2003; the China Securities Regulatory Commission’s (CSRC) Code of Corporate Governance for Listed Companies in China, in 2001, and, in Indonesia, the National Committee on Corporate Governance (NCCG) the Indonesian Code for Good Corporate Governance, in 2001. The OECD revised its Principles of Corporate Governance Codes in 2004, and Australia and Indonesia also introduced their revised codes in 2007 and 2006 respectively. In 2006, the name of the National Committee on Corporate Governance in Indonesia was also changed to National Committee on Governance and its functions expanded to include oversight of corporate governance practices in both the public sector and the private sector (National Committee on Governance, 2006).

To be able to draw upon previous studies on the implementation of the Codes in these three countries, this paper has chosen to mainly base its comparison on the earlier version of the Corporate Governance Codes in Australia and Indonesia, i.e. the Australian Principles of Good Governance and Best Practices Recommendations (2003 version) and the Indonesian Code for Good Corporate Governance (2001 version). To keep this paper current, major revision in the latest Corporate Governance Codes in Australia and Indonesia are also discussed to a certain extent. Overall, this paper explores the similarities and differences of corporate governance codes in these three countries under their dramatically different legal, social and economic framework and it also reviews whether the codes are effective in encouraging good corporate governance behaviour in listed companies.

OVERVIEW

Corporate governance codes in each country are formulated according to its legal, social and economic framework. To a certain extent, the codes also reflect the corporate structure in each country. Part of the reason to compare the Codes of Australia, China and Indonesia is that each country has a corporate sector with its own characteristics. Compared with the corporate sector in China and Indonesia, the corporate sector in Australia is represented by a somewhat dispersed share ownership structure. However, in recent years, there is evidence suggesting that there is a growing trend of institutional investor involvement (Ramsay and Blair, 1993; Lamba and Stapledon, 2001). While China and Indonesia are both developing countries, each of them has developed a corporate sector which has its own characteristics. The structure of China's corporate sector is unique as the government – the major shareholder, controls most listed companies. On the other hand, Indonesia's corporate sector is mainly dominated by family businesses (LaPorta et al., 1998; Claessens et al., 2000) and its economy is also more or less controlled by a few powerful families (Tabalujan, 2002).

Apart from corporate structures, Australia, China and Indonesia are also alleged to belong to different corporate governance models. Corporate governance models around the world can be categorised into two major types, the outsider-based model and the insider-based model (Mayer, 1994). The outsider-based model is represented by the model in the US and the UK, where there is a dispersed ownership structure; the insider-based model is represented by the model in Germany and Japan with a more concentrated ownership structure (Charkham, 1995). Conventional wisdom often treats the corporate governance model in Australia as an outsider-based model (Cheffins, 2002) and the corporate governance model in China as an insider-based model (Tam, 1999; Jia, 2004). Due to the concentration of family ownership in Indonesia's corporate sector, the corporate governance model in Indonesia can be branded as one type of the insider-based model (Tabalujan, 2002). The differences in the corporate sectors in these three countries provided the basis for us to compare the corporate governance codes in these three countries.

CORPORATE GOVERNANCE CODES AND PRINCIPLES IN AUSTRALIA, CHINA AND INDONESIA

Australia

Among the corporate governance codes/principles adopted by Australia, China and Indonesia, the Principles of Corporate Governance, issued by the ASX Corporate Governance Council, are the most comprehensive. The code covers 10 major principles ranging from respecting the rights of shareholders to promoting ethical and responsible decision-making, risk management and, properly addressing the interests of other stakeholders. Armstrong (2004) has provided a more detailed discussion on the Australian Principles.

China

In order to improve corporate governance in its listed companies (most of them transformed from state-owned enterprises), China introduced its Code of Corporate Governance for Listed Companies in China in 2001. Mainly adapted from the OECD principles (Tomasic, 2005), its major areas also covers issues related to the controlling shareholders (mainly state-owned enterprises) and their roles n corporate governance.

Indonesia

Indonesia's Code is also more or less modelled from the OECD principles of corporate governance. It also covers major areas related to respecting shareholder's rights and the composition and functions of a board of directors. The World Bank has provided a comprehensive analysis of the degree of observance of the Indonesian Code to the OECD Principles (World Bank, 2004).

In order to analyse the differences and similarities of corporate governance codes in these three countries, this paper has engaged in content analysis by looking closely at these three sets of codes, using a descriptive method. s *Table 1* below provides a summary on the major sections of the codes/principles in these three countries.

Table 1. Similarities among corporate governance codes in Australia, China and Indonesia

	China	**Indonesia (2001 version)**	**Australia (2003 version)**
Shareholder's right	"shareholders shall enjoy the legal rights stipulated by laws, administrative regulations and the company's articles of association" (P 1 of the China Code)	"The rights of shareholders shall be protected and, accordingly, shareholders shall be able to exercise their rights through reliance upon appropriate procedures that have been adopted by the Company concerned, which procedures shall be required under applicable regulations having the force of law" (P 2 of the Indonesia Code)	"Companies should respect the rights of shareholders and facilitate the effective exercise of those rights. (P 28 in its revised version of the Australian Principle)
Establishment of board committees: What committees are recommended	See P 7 of the China Code, the board of directors of a company may establish the following committees: - a corporate strategy committee - an audit committee - a nomination committee - a remuneration and appraisal committee - other special committees in accordance with the resolutions of the shareholders' meetings	See P 11 of the China Code, the following committees could be established in the board: - Nomination committee - Remuneration committee - Insurance committee - Audit committee	The establishment of board committees are recommended in various area of the Principle as it fits within the document. Overall, the following committees should be established: - audit committee - nomination committee - risk management committee - remuneration committee
Introduction of independent director	See chapter 3 (4) of the China Code: 'a listed company shall introduce independent directors to its board of directors in accordance with relevant regulations.'	See Section 3.2 on P 12 of the Indonesia Code: 'Depending on the specific character of the Company, at least 20% of the members of the Direksi[1] should be "outside directors" as mentioned in section 2.2 in order to increase the	See Australia Principle recommendation 2.1: 'A majority of the board should be independent director

[1] Direksi means director
[2] Dewan Komisaris means Board of Commissioners.

	China	Indonesia (2001 version)	Australia (2003 version)
		effectiveness of its management role, and the transparency of its deliberations. Such members of the Direksi shall be independent from the Dewan Komisaris[2] and controlling shareholders.'	
Establishment of a supervisory board	As stated in the China Code, apart from a management board, each company also has a supervisory board who oversees the function of the management board	In Indonesia's case, there is a board of commissioners (DEWAN KOMISARIS), who perform the similar duty of the supervisory board as is the case of China – See P 6 of the Indonesia Code	No such requirement.
Recognising the interest of major stakeholders	Chapter 6 of the China Code is specifically devoted to the protection of stakeholder interest.	Section VI of the Indonesia Code is focused on stakeholder interest.	In Australia Principle 3, it was specifically mentioned that ethical and responsible decision-making includes taking into consideration of stakeholders' interest.
Risk Management	No comprehensive coverage	No comprehensive coverage	Comprehensive coverage, see Principle 7: Recognise and manage risk (only in 2007 version)

*This table was complied based on Corporate governance codes and principles in China (China Securities Regulatory Commission, 2002), Indonesia (National Committee on Corporate Governance, 2001; National Committee on Governance, 2006) and Australia (ASX Corporate Governance Council, 2003, 2007).

ANALYSIS

Despite the differences in ownership structure in listed companies in Australia, China and Indonesia, there are some similarities among the codes in these three countries. They are: an emphasis on shareholder rights, the committee structures, the inclusion of independent (outside) directors and their implementation (Table 1). The Chinese and Indonesian Codes also have several similarities. In particular, both of them required companies not only to establish a board of directors, but also to appoint a supervisory board in China and a board of commissioners in Indonesia (in Indonesia's case, the board of commissioners is the equivalent of the supervisory board in China).

Despite the similarities in their origins and content, there are some major differences in the corporate governance codes of these three countries. For example, in the Code of Corporate Governance issued by the China Securities and Regulatory Commission (CSRC), disclosure of related party transactions and major shareholders' interests are specifically addressed and there is also a designated chapter (chapter 2) on proper management of relationships between listed companies and their controlling shareholders (Tomasic, 2005). This was certainly closely related to the unique corporate structure in China, in which most listed companies have a controlling shareholder (often the controlling shareholder is a state-owned enterprise). The historical relationship between a controlling shareholder and a listed company means that there is always a blurred line between the roles and responsibilities of a listed entity and its controlling shareholder (Jia, 2005). In order to promote good governance behaviour, it is important for the Code of Corporate Governance in China to emphasise the importance of keeping the controlling shareholder and the listed entity independent.

In Australia, since the introduction of the Corporate Governance Principles in 2003, most listed companies have started to publish a governance report. Several companies (e.g. ANZ, Shell, BP) also distributed additional reports related to environmental management.

Australia has taken a leading role in updating its Principles of Corporate Governance to keep pace with the latest development in the corporate world. nce in 2003 in recent years, the general public has demanded that corporations be more aware of their social responsibilities and be good s. In order to change the corporate governance codes discussions have been undertaken in 2006 to update the Principles of Corporate Governance Codes issued in 2003. The latest revision of the principles was issued in August 2007(ASX Corporate Governance Council, 2007) and in the revision, the ASX has expanded on practical issues such as risk management and the introduction of a Code of Conduct to encourage ethical behaviour. This is generally with the practices in major corporations. Most S&P 300 companies now have a Code of Conduct and a majority of them published their Codes of Conduct on their website; which in a way illustrated the level of transparency of their corporate governance practices.

In Indonesia's case, its Code for Good Corporate Governance (issued in 2001) was also updated in 2006. To help with the implementation of its corporate governance code, its 2006 version also emphasised the importance of business ethics and the formation of a proper Code of Conduct.

In terms of the compliance with the Code, empirical research has shown that corporate governance codes in each country have been complied with at least "in form". Research conducted by Reputex of S&P 300 companies suggested that in terms of corporate governance practices and compliance, at least a third of these 300 companies have achieved an above satisfactory result (RepuTex, 2006). In China's case, despite being criticised as "box ticking" with its corporate governance practices (Haddock et al., 2003; Allen, 2000), a review of the 2002 annual reports of 74 leading companies in China have shown considerable compliance with the requirements of the corporate governance codes in terms of reporting (Jia, 2005). For Indonesia, a study conducted by Standard & Poor's and Corporate Governance and Financial Reporting Centre (2004) also shown that most of the 45 companies studied have disclosed the name of their directors and commissioners as well as their corporate governance practices in their 2002 annual report.

CONCLUSION

To summarise, the code in these three countries have much in common. They have similar origins and a similar aim: to improve corporate governance with the objectives of being more efficient, increasing accountability and disclosure and at the same time enhancing shareholder confidence in the stock markets.

While the codes among these three countries have similarities and differences, which is suited to each country's unique circumstances, this paper also demonstrated that corporate governance codes have at least encouraged compliance behaviour among listed companies to formally report their corporate governance practices. Despite most companies' corporate governance report being only "in form" rather than "in substance", it demonstrated that the corporate governance codes have encouraged some good governance compliances behaviour in getting the governance structure right, which is an important step in working toward really practice good corporate governance in listed companies.

This paper also illustrates that the adoption of governance principles is clearly influenced by different ownership structures, and variations in legal and political frameworks. Companies from Australia doing business with their Asian neighbours will have to take account of government influences in China and private interests in Indonesia. The Asian companies investing in Australia will need to take note of the attention given in Australia to ‘nonmaterial risks’ reflected in the interests of stakeholders other than shareholders.

Understanding the similarities and differences in corporate governance codes in these three countries is essential for the many international companies operating across these three jurisdictions. This paper meets this need by presenting an overview of the governance structures in the three countries, describing the similarities and analyses the differences, and drawing some conclusions about their influence on international trade.

REFERENCES

Allen, J. 2000, 'Code convergence in Asia: smoke or fire?' *Corporate Governance International*, vol.1, pp.23-37.

Armstrong, A. 2004, 'Corporate governance standards: intangibles and their tangible value', *Australian Journal of Corporate Law*, vol.17, no.1, pp.97-110.

ASX Corporate Governance Council 2003, *Principles of good corporate governance and best practice recommendations*, Australian Stock Exchange, [Online]. Available: http://www.jacmac.com.au/publications/qy8_01_.pdf Accessed 15 June 2004

ASX Corporate Governance Council 2007, *Corporate governance principles and recommendations, 2nd version*, [Online]. Available: http://www.asx.com.au/supervision/governance/Revised_Corporate_Governance_Principles_and_Recommendations.htm Accessed 10 October 2007

Berle, A. A. and Means, G. C. 1932, *The modern corporation and private property*, Macmillan, New York.

Charkham, J. P. 1995, *Keeping good company : a study of corporate governance in five countries*, Oxford University Press, Oxford.

Cheffins, B. R. 2002, 'Comparative corporate governance and the Australian experience' In Ramsay, I. (ed.) *Key developments in corporate law and trusts law: essays in honour of Professor Harold Ford*, LexisNexis Butterworths, Sydney, pp. 13-38.

China Securities Regulatory Commission 2002, *Code of corporate governance for listed companies in China*, [Online]. Available: http://www.csrc.gov.cn/ Accessed 27 February 2004

Claessens, S., Djankov, S. and Lang, L. H. P. 2000, 'The separation of ownership and control in East Asian Corporations', *Journal of Financial Economics*, vol.58, pp.81-112.

Farrar, J. H. 2005, *Corporate governance: theories, principles, and practice*, 2nd, Oxford University Press, Melbourne.

Haddock, F., Chow, O. and Law, R. 2003, 'Talking the talk', *Asiamoney*, vol.14, no.7,

Jia, X. 2004, *An overview of corporate governance models: what are the implications for China and Australia*, University of Otago, Available: Accessed

Jia, X. 2005, 'Governing China's listed companies: annual reports and the role of the PRC code of corporate governance', *Australian Journal of Corporate Law*, vol.18, no.3, pp.233-242.

Lamba, A. S. and Stapledon, G. P. 2001, *The Determinants of Corporate Ownership Structure: Australian Evidence*, [Online]. Available: http://ssrn.com/abstract=279015 Accessed 11 September 2004

LaPorta, R., Lopez-de-Silances, F., Shleifer, A. and Vishny, R. W. 1998, 'Law and finance', *Journal of Political Economy*, vol.106, no.6, pp.1113-1155.

Mayer, C. 1994, 'Stock-markets, financial institutions, and corporate performance' In Dimsdale, N. and Prevezer, M. (ed.) *Capital markets and corporate governance*, Clarendon Press, Oxford, pp. 179-194.

National Committee on Corporate Governance 2001, *Indonesian Code for Corporate Governance*, [Online]. Available: http://www.ecgi.org/codes/documents/indon_2001.pdf Accessed 25 June 2007

National Committee on Governance 2006, *Indonesia's code of corporate governance*, [Online]. Available: http://www.ecgi.org/codes/documents/indonesia_cg_2006_en.pdf Accessed 10 October 2007

OECD 2004, *OECD principles of corporate governance*, [Online]. Available:

http://www.oecd.org/dataoecd/32/18/31557724.pdf
Accessed 6 November 2004

Rafferty, M. 1999, 'Corporation' In (ed.) *Encyclopedia of political economy*, Taylor & Francis, London, pp. 154-157.

Ramsay, I. and Blair, M. M. 1993, 'Ownership concentration, institutional investment and corporate governance: an empirical investigation of 100 Australian companies', *Melbourne University Law Review*, vol.19, pp.153-194.

RepuTex 2006, *RepuTex Governance Leaders Index*, [Online]. Available: http://www.reputex.com.au/subcat.asp?id=146&cid=8
Accessed 10 October 2007

standards & Poor's and Corporate Governance and Financial Reporting Centre 2004, *Corporate governance disclosures in Indonesia: a study of LQ 45 companies*, [Online]. Available:
http://www.cgfrc.nus.edu.sg/publications/cg_dis_indon.htm
Accessed 10 October 2007

Tabalujan, B. 2002, 'Family capitalism and corporate governance of family-controlled listed companies in Indonesia', *Univeristy of New South Wales Law Journal*, vol.25, no.2, pp.486-514.

Tam, O. K. 1999, *The development of corporate governance in China*, Edward Elgar Publishing, Northampton, Ma.

Tomasic, R. 2005, 'Comparing corporate governance principles: China, Australia and OECD' In Tomasic, R., Wang, F., Zhao, X. and Ma, Z. (ed.) *Corporate governance: challenges for China*, Law Press, Beijing, pp. 1-32.

World Bank 2004, *Report on the observance of standards and codes (ROSC) corporate governance country assessment: Republic of Indonesia*, [Online]. Available: http://www.worldbank.org/ifa/rosc_cg_idn.pdf
Accessed 27 June 2007

Zingales, L. 1998, 'Corporate governance' In P Newman (ed.) *The new Palgrave dictionary of economics and law*, Macmillan Reference, London, pp. 497-503.